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Making Assignments For The Benefit Of Creditors As Easy As A-B-C

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MAKING ASSIGNMENTS FOR THE BENEFIT OF CREDITORS AS EASY AS A-B-C

*Carly Landon**

Introduction	1452
I. Understanding the Basics of Assignments for the Benefit of Creditors	1456
A. What Is an Assignment for the Benefit of Creditors?	1456
B. How Do ABCs Work?	1458
C. How ABCs Fit into the Bigger Insolvency Picture: Comparing ABCs to Chapter 7 and Chapter 11 Bankruptcy.....	1462
1. Chapter 11 Bankruptcy.....	1463
2. Chapter 7 Bankruptcy.....	1464
3. Advantages of ABCs over Federal Bankruptcy	1466
4. Disadvantages of ABCs over Bankruptcy.....	1467
D. A Brief History of ABCs and Their Reform	1469
II. A Spectrum of ABCs and Comparing the Various Forms Across the States.....	1471
A. States with Common Law ABCs.....	1472
B. States with Minimally Regulated ABC Processes.....	1475
C. States with Heavily Regulated ABC Forms	1478
III. Making ABCs a Viable Alternative to Bankruptcy Throughout the States.....	1482
A. States Need to Reform ABCs but Maintain Minimum Statutory Regulation	1483
B. While Minimally Regulated ABCs Are Not Perfect, they Provide the Best Opportunity for ABCs to See More Frequent Use.....	1486
C. Legal Education, Including Law School Classes and CLE Programs, Ought to Adjust Their Curriculum to Include Instruction on ABCs in Order to Make	

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Reforms as Successful as Possible and Make ABCs an Alternative to Be Considered.....	1487
Conclusion.....	1488

INTRODUCTION

Small business ownership remains the American dream,¹ inspiring many Americans to create their own businesses—there are nearly 550,000 new start-ups each month.² These start-ups create new jobs and occasionally spur the beginning of new industries.³

Unfortunately, however, not all new start-ups succeed. It is common for start-up businesses to fail in their first years of existence.⁴ In fact, according to the United States Small Business Administration (SBA), “[Twenty] percent of all small businesses survive the first year, [thirty] percent survive the second year, and half survive the first five years.”⁵ Further, while seventy percent of new businesses survive at least two years, this rate drops to fifty percent by the five-year mark and thirty-three percent at the ten-year point, with just twenty-five percent of all new businesses lasting fifteen years or more.⁶

Many new business owners thus find themselves consulting lawyers about how to handle business failure.⁷ More often than not, lawyers recommend filing for bankruptcy.⁸ Although bankruptcy is frequently the default response, it is not the only option. For financially troubled companies, one size does not fit all.⁹ In 2003, of

1. Bob Llewellyn, *What Is the American Dream?*, SAFE INVESTOR (Jan. 2003), <http://www.thesafeinvestor.com/articles/articleTheAmericanDream.pdf>.

2. Jennifer Bury, *The New American Dream is Not Owning a House but Owning Your Own Business*, MARKETING DEPT. FRANCHISE BLOG (Jan. 30, 2012, 12:42 P.M.), <http://www.tmdfranchise.com/blog/bid/121379/The-New-American-Dream-is-not-owning-a-House-but-owning-your-Own-Business>.

3. U.S. SMALL BUS. ASS'N OFFICE OF ADVOCACY, FREQUENTLY ASKED QUESTIONS (2012), *available at* http://www.sba.gov/sites/default/files/FAQ_Sept_2012.pdf.

4. *Id.*; MICHAEL G. WILLIAMSON, THE ABCs OF BUSINESS LIQUIDATIONS—A FLEXIBLE ALTERNATIVE TO BANKRUPTCY (2013), *available at* http://html.documation.com/cds/NCBJ2011/assets/PDFs/XIII_C.pdf.

5. *SBA Helps Parkersburg Small Business Beat First Year Failure Statistic*, U.S. SMALL BUS. ADMIN., <http://www.sba.gov/content/sba-helps-parkersburg-small-business-beat-first-year-failure-statistic> (last visited Mar. 29, 2014).

6. U.S. SMALL BUS. ASS'N OFFICE OF ADVOCACY, *supra* note 3.

7. WILLIAMSON, *supra* note 4.

8. *Id.*

9. Bob Eisenbach, *Assignment for the Benefit of Creditors: Simple as ABC?*, BUSINESS BANKR. BLOG (Mar. 16, 2008, 11:38 PM), <http://bankruptcy.cooley.com/>

almost 550,000 failing small businesses, only 34,000 filed for bankruptcy.¹⁰ What happened to the other ninety-four percent of these businesses? Some scholars have attempted to answer this question by inferring that the “vast majority of small businesses resolve distress under state law” in a process called an “assignment for the benefit of creditors” (ABC).¹¹

ABCs provide a state-law alternative to the filing of a federal bankruptcy case. Aptly named, they involve the assignment of an insolvent company’s assets to a third-party assignee, who is selected by the company and charged with the duty of liquidating the company’s assets to satisfy creditors’ claims against the company.¹² In recent years, states such as California, Florida, Illinois and Massachusetts have seen frequent use of ABCs; in the majority of states, however, ABCs are routinely passed up for bankruptcy and its other alternatives.¹³

Despite the varying frequency of use across the states, ABCs have become much more commonplace since the turn of the twenty-first century as venture-capital and private-equity firms saw investments in high-tech, dot-com companies fail at an enormous rate.¹⁴ In the early 2000s, many California dot-com and technology companies used the California ABC to deal with the collapse of the dot-com industry.¹⁵

2008/03/articles/business-bankruptcy-issues/assignments-for-the-benefit-of-creditors-simple-as-abc.

10. *Id.*

11. See William Choslovsky & Eric Walker, *An Alternative to Bankruptcy: the ABCs of ABCs*, in THE AMERICAS RESTRUCTURING & INSOLVENCY GUIDE 2008/2009, at 90, 91 (2009), available at http://www.americasrestructuring.com/08_SF/p90-95%20An%20alternative%20to%20bankruptcy.pdf (although ABCs likely account for a percentage of these companies that are no longer in business, other out-of-court workouts are also responsible); Edward R. Morrison, *Bargaining Around Bankruptcy: Small Business Workouts and State Law*, 38 J. LEGAL STUD. 255, 255 (2009).

12. See Choslovsky & Walker, *supra* note 11, at 91–92.

13. Robert Richards & Nancy Ross, *Practical Issues in Assignments for the Benefit of Creditors*, 17 AM. BANK. INST. L. REV. 5, 5 (2009); see also Morrison, *supra* note 11, at 257 (“One state procedure, the ABC, is nearly as popular as federal bankruptcy law.”).

14. GEOFFREY BERMAN, GENERAL ASSIGNMENTS FOR THE BENEFITS OF CREDITORS: THE ABCs OF ABCs, at vii (2d ed. 2006).

15. Vivian Luo, *A Preference for States? The Woes of Preempting State Preference Statutes*, 24 BANKR. DEV. J. 513, 513 (2008); COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, N.Y.C. BAR, NON-BANKRUPTCY ALTERNATIVES TO RESTRUCTURING AND ASSET SALES 12 (2010), available at <http://www.nycbar.org/pdf/report/uploads/20072001-NonBankruptcyAlternativestoRestructuringsandAssetSales.pdf>.

As a result, California became the “capital of ABCs” during the dot-com meltdown.¹⁶ The management of a deteriorating dot-com or other failing technology company often required a faster and more cost-efficient process than bankruptcy so that it could “engage in last-ditch efforts to sell the business in the face of mounting debt.”¹⁷ Potential buyers of those companies, on the other hand, were only willing to move forward if they were able to continue producing and using the technology assets of the insolvent company.¹⁸ Thus, these companies needed to work fast to assure that certain key employees, whose departure from the company would greatly diminish the value of the firm and its assets, would continue working for the successor company and would not look elsewhere for jobs.¹⁹ Time was of the essence for these companies because the more time that passed, the more likely that those key employees would find other employment.²⁰

Interested buyers were also often only willing to move forward if they could be assured that they would be free of liability from unsecured debt of the insolvent company.²¹ ABCs were ideal for addressing these unsecured debt and time issues because “the assignee [could] act more quickly; the assignee [was] likely to be more experienced at dealing with technology-related assets; and the use of an assignee [involved] lower transaction costs.”²²

Moreover, the benefits of ABCs over bankruptcy are not confined to only dot-com and technology industries, or even to the past. After credit markets experienced a dramatic increase in defaults in the second half of 2007, many expected an increase in corporate federal bankruptcy filings.²³ Nevertheless, business bankruptcy filings dropped significantly in the period since 2008, specifically in the commercial context.²⁴ Some theorize that this low number of filings

16. David S. Kupetz, *Assignment for the Benefit of Creditors: Effective Tool for Selling and Winding Up Distressed Businesses*, VALLEY LAW., June 2013, at 34, 35.

17. David Kupetz, *Assignment for the Benefit of Creditors: Exit Vehicle of Choice for Many Dot-Com, Technology, and Other Troubled Enterprises*, 11 J. BANKR. L. & PRAC. 71, 81–82 (2001).

18. *Id.*

19. *Id.*

20. *Id.*

21. *Id.*

22. Ronald J. Mann, *An Empirical Investigation of Liquidation Choices of Failed High Tech Firms*, 82 WASH. U. L. REV. 1375, 1390 (2004).

23. Choslovsky & Walker, *supra* note 11, at 90.

24. See *Bankruptcy Filings Through First Three Quarters of 2013 Fall 13 Percent from 2012, Commercial Filings Fall 23 Percent*, AM. BANKR. INST. (Oct. 3, 2013), <http://news.abi.org/press-releases/bankruptcy-filings-through-first-three-quarters-of-2013-fall-13-percent-from-2012-com; Percent Change in Bankruptcy Filings, 2011–>

can be explained, in part, by small business debtors relying on simpler ABC practices rather than federal bankruptcy.²⁵

Today, the debate about the advantages of bankruptcy versus ABCs remains urgent.²⁶ In light of the many advantages of ABCs to small businesses, which are not limited to technology industries, it is surprising that ABCs have not seen more widespread use outside of a select few states. ABCs are currently in a unique position because they have become “particularized to fit the needs of those states that have found the process a useful tool.”²⁷ In doing so, ABCs have become so diverse on a state-by-state basis²⁸ that the divide between the states that find ABCs to be a useful tool and the states that rarely, if ever, use ABCs has increased and will continue to increase if no reform occurs.

This Note evaluates the different approaches to ABCs across the states, and suggests that these procedures can be used in a wider range of companies, especially if states reform their current ABC laws. It argues that a state would enhance the benefits of ABCs and minimize the current disadvantages if it were to adopt a minimally regulated ABC. Part I begins by explaining the process of an ABC, its differences from bankruptcy, and the varying frequency of its use amongst the states. Part II sorts the varying forms of ABCs into three categories to address the positive and negative aspects of each of these ABCs and explain three general forms in which ABCs are found. Finally, Part III proposes reforms to increase reliance on ABCs throughout all states. This Note concludes by arguing that adopting a minimally regulated ABC form, like the ABC found in California, offers the best solution after which to model ABC reforms.

2013, U.S. COURTS, <http://www.uscourts.gov/Statistics/BankruptcyStatistics/interactive-map.aspx> (last visited Apr. 15, 2014); *U.S. Bankruptcy Courts Bankruptcy Cases Filed, Terminated, and Pending, Fiscal Years 2008–2012*, U.S. COURTS, <http://www.uscourts.gov/Statistics/JudicialBusiness/2012/us-bankruptcy-courts.aspx> (last visited Apr. 15, 2014).

25. See, e.g., Choslovsky & Walker, *supra* note 11, at 91; Morrison, *supra* note 11, at 255.

26. See Gordon Eng, *Going Out of Business: Practitioners Need to Consider the Advantages of Formal Bankruptcy to Other Means of Closing a Business*, 32 L.A. LAW. 32, 33–35 (2009).

27. Geoffrey Berman & Catherine E. Vance, *Relief without a Petition: Non-Bankruptcy Alternatives: Model Statute for General Assignments for the Benefit of Creditors: the Genesis of Change*, 17 AM. BANKR. INST. L. REV. 33, 33 (2009).

28. *Id.*

I. UNDERSTANDING THE BASICS OF ASSIGNMENTS FOR THE BENEFIT OF CREDITORS

This Part explains what ABCs are and how the ABC process works. It also briefly explains how ABCs differ from federal bankruptcy proceedings, particularly Chapter 11 and Chapter 7 bankruptcy cases. Using federal bankruptcy as a point of comparison, this Part explores the advantages and disadvantages of ABCs to demonstrate those types of companies that would especially benefit from the ABC process. This Part finally provides a brief history of ABCs, and discusses ABCs in their current use and form.

A. What Is an Assignment for the Benefit of Creditors?

ABCs are the state or common law alternatives to bankruptcy, which trace their roots back to English common law.²⁹ ABC statutes today may supersede common law assignments entirely, or merely supplement them, allowing common law assignments to continue.³⁰ Black's Law Dictionary defines a "general assignment for the benefit of creditors" as "a transfer of legal and equitable title to all debtor's property to a trustee, with authority to liquidate the debtor's affairs and distribute proceeds equitably to creditors."³¹ An ABC is a business liquidation device available to an insolvent debtor as an alternative to bankruptcy proceedings.³² However, "ABCs are not limited to liquidations. Just as in bankruptcy, an ABC can be used to facilitate a going-concern sale of the debtor's assets to a third-party."³³ Basically, ABCs are used as a vehicle for the sale or liquidation of a business in an orderly, controlled way.³⁴ It is important to note that ABCs are not used to turn a business around, restructure, or financially rehabilitate the business. Rather, ABCs are purely used to wind the business down by selling or liquidating it.³⁵

At the risk of oversimplifying the process, an ABC involves a trust arrangement in which an insolvent business assigns its assets to an

29. See DEBTOR-CREDITOR LAW § 35.03 (Theodore Eisenberg ed., 2014).

30. Neil V. Verbrugge, *The "ABC's" of Hawaii's Assignment for Benefit of Creditors Law*, 13 HAW. B. J. 127, 127 (2009).

31. BLACK'S LAW DICTIONARY (9th ed. 2009).

32. See Kupetz, *supra* note 16, at 35.

33. Choslovsky & Walker, *supra* note 11, at 92.

34. *E.g.*, BERMAN, *supra* note 14, at 1; Richards & Ross, *supra* note 13, at 5.

35. See Kupetz, *supra* note 16, at 35; Matthew S. Barr & Peter K. Newman, *Examining Assignments for the Benefit of Creditors*, L. 360 (May 1, 2013), <http://www.law360.com/articles/433794/examining-assignments-for-the-benefit-of-creditors> (password required); BERMAN, *supra* note 14, at 3.

assignee, i.e. the trustee, who then holds property for the benefit of a special group of beneficiaries, i.e. the creditors.³⁶ Some suggest ABCs are the “functional equivalent” of liquidation under Chapter 7 of the U.S. Bankruptcy Code.³⁷ However, bankruptcy holds distinct federal advantages over ABCs.³⁸ For example, it imposes an automatic stay, allows for avoidance of preferential transfer, and may grant a discharge to an individual debtor—for example, a sole proprietor.³⁹ Further, ABCs have become particularized to fit the needs of those states that have found the process of a useful tool in managing debtor-creditor relationships and as a vehicle for the orderly liquidation of a business outside of bankruptcy.⁴⁰

ABCs are generally used in two scenarios.⁴¹ In the first, similar to a Chapter 7 bankruptcy, the company is unable to continue operating throughout the insolvency process and it cannot find a buyer for the company.⁴² Using an ABC, the insolvent business’s assets are liquidated, accounts receivable are collected, and distributions are made to creditors.⁴³ In the second scenario, there is a potential buyer for the failing business, but not enough cash to justify the time and expense associated with a Chapter 11 bankruptcy.⁴⁴ As a result, the

36. See, e.g., *In re Sundance Corp.*, 83 B.R. 746, 748 (Bankr. D. Mont. 1988) (“An assignee for the benefit of creditors is one to whom, under an insolvent or bankrupt law, the whole estate of a debtor is voluntarily transferred to be administered *for the benefit of creditors*.” (emphasis added)); *Paul H. Schwendener, Inc. v. Jupiter Elec. Co.*, 829 N.E.2d 818, 827–28 (Ill. App. Ct. 2005) (explaining “an assignment for the benefit of creditors is simply a unique trust arrangement in which the assignee (or trustee) holds property for the benefit of a special group of beneficiaries, the creditors” (internal quotation marks omitted)); BERMAN, *supra* note 14, at 3; Choslovsky & Walker, *supra* note 11, at 91; Williamson, *supra* note 4.

37. BERMAN, *supra* note 14, at 1.

38. See generally, BERMAN, *supra* note 14, at 4–7; Jeffrey Davis, *Florida’s Beefed Up Assignment of the Benefit of Creditors*, 19 U. FLA. J.L. & PUB. POL’Y 17, 33 (2008) (“Bankruptcy, with all its complexity and formality, is a much more powerful process than an assignment for the benefit of creditors. Where there is a need for that power, it is the superior choice. Examples are: 1) where there is an immediate need for the automatic stay, 2) where the debtor is engaged in significant multi-state operations, 3) where assets are located in numerous states, 4) where the debtor’s corporate structure is complex, 5) where the debtor has made large preferential transfers to outsiders, 6) where there is potential liability for environmental or other future claims, or 7) where successors have a high risk of liability.”).

39. 28 U.S.C. § 1334(e) (2012); see also 11 U.S.C. § 362(a) (2012).

40. See Berman & Vance, *supra* note 27, at 33–34.

41. See *Assignments for the Benefit of Creditors*, ROSEN, P.A., <http://www.rosenpa.com/Articles/Assignment-for-the-Benefit-of-Creditors-in-Florida.shtml> (last visited Mar. 5, 2013).

42. *Id.*

43. *Id.*

44. *Id.*

company chooses an ABC over bankruptcy in the interests of saving time and money.⁴⁵ Whether used to wind down the company or accomplish the sale of a troubled company, ABCs can work to maximize a creditor's recovery from the assets of the distressed debtor.⁴⁶

B. How Do ABCs Work?

Because of differences in state law⁴⁷ and the circumstantial differences of each business, ABC processes are never identical; however, each assignment overall involves the same basic principles.⁴⁸ To commence the ABC process, a distressed corporation will generally need to "obtain both board of director authorization and shareholder approval."⁴⁹ Although ABCs are a state law procedure, many of their requirements, such as board and shareholder approval, are rooted in state corporate law rather than in ABC statutes or ABC common law.⁵⁰ Courts generally apply either the corporate law of the state in which the debtor is incorporated, the state law of the assignor's domicile, or the law of the state where the assignment is made.⁵¹ Next, the distressed entity (the "debtor" or "assignor")

45. *Id.*

46. See Kupetz, *supra* note 16, at 34.

47. See *supra* Part II. The differences between ABCs across the states will be covered in depth later. The purpose of this subpart is to provide background information so that the information later can be better understood. It is useful to note, however, that the differences between categories of ABCs are most visible during the ABC process. For example, whether an ABC is judicial or non-judicial in addition to the amount of judicial involvement is crucial to how that state's ABC is categorized. Additionally, the distribution scheme of ABCs, i.e. notice deadlines and priority schemes, can also affect the process.

48. Berman, *supra* note 14, at 6.

49. See Kupetz, *supra* note 16, at 35 ("The ABC constitutes a transfer of all of the assignor's assets to the assignee and the law of many states provides that the transfer of all of a corporation's assets is subject to shareholder approval (although this approval may be obtained, in some instances, retroactively).").

50. *C.f.*, Berman, *supra* note 14, at 1 (saying ABCs are subject to the laws of the state in which the assignment takes place); COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 10 (explaining how corporate law can impact the ABC process); Leslie R. Horowitz & John A. Lapinski, *Advising Distressed Businesses on an Alternative to Bankruptcy*, L.A. LAW., Sept. 2001, at 18, available at <http://www.lacba.org/Files/LAL/Vol24No6/977.pdf>; Richards & Ross, *supra* note 13, at 8–9; Scott E. Blakely, *Say Goodbye to the State Preference Action*, COVERING BUS. CREDIT, http://www.coveringcredit.com/business_credit_articles/Bankruptcy/art708.shtml (last visited Apr. 15, 2014).

51. See *Judd v. J.W. Forsinger Co.*, 186 A. 525, 526–27 (N.J. 1936); DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03; Horowitz & Lapinski, *supra* note 50, at 18; Richards & Ross, *supra* note 13, at 8–9 (stating that courts apply the law of the "state of incorporation" to corporations filing for ABCs).

enters into an agreement with the assignee⁵² where the debtor will transfer its estate in trust (i.e., all of its rights, title, interest in, and custody and control of its property) to the assignee.⁵³ The transfer of these assets is subject to all existing liens so the assignee is “bound to honor all valid, i.e. perfected and enforceable, liens.”⁵⁴ Further, in some states, before any significant event can take place or the agreement can be executed, the assignment agreement must be filed with the court, and in some states, it must also be court approved, which could entail a hearing.⁵⁵

Because the assignee is crucial to the ABC process, it is worth explaining who the assignee is and what his or her function is. As stated previously, an assignee for the benefit of creditors is one to whom “the whole estate of a debtor is voluntarily transferred to be administered *for the benefit of creditors*.”⁵⁶ The assignee is generally a disinterested third party who is not related to the debtor and who has experience liquidating businesses.⁵⁷ Often, especially in states where ABCs are more common, assignees have expertise in the debtor’s industry.⁵⁸ For example, many of the assignors used in ABCs following the crash of the dot-com industry had expertise in the technology industry so they understood how to best value and liquidate the assets particular to a dot-com business.⁵⁹ The assignee becomes a fiduciary on behalf of any and all creditors of the debtor, as well as for the debtor, and ultimately, its owner and shareholders.⁶⁰

Before the assignee can liquidate the assets and distribute the proceeds, he or she needs to know what assets comprise the assignment estate and who has a claim against the assets of the

52. See Richard H.W. Maloy, *The “Priority Statute”—The United States’ “Ace-in-the-Hole,”* 39 J. MARSHALL L. REV. 1205, 1278 (2006) (indicating that terms “assignee” or “trustee” are used interchangeably to define “person to whom the assignment has been made”).

53. See *Moecker v. Antoine*, 845 So. 2d 904, 910 (Fla. Dist. Ct. App. 2003) (noting that in ABCs the “debtor voluntarily assigns its assets to a third party as trustee for the purpose of liquidating the assets to satisfy, in full or in part, creditors’ claims against the debtor”); BERMAN, *supra* note 14, at 6 (“The execution and acceptance of the assignment contract creates an ‘estate,’ which includes the transferred assets and the proceeds thereof, subject to the claims of the assignor’s creditors.”); Kupetz, *supra* note 16, at 34–35.

54. BERMAN, *supra* note 14, at 4.

55. *Id.*

56. *In re Sundance Corp.*, 83 B.R. 746, 748 (Bankr. D. Mont. 1988) (emphasis added).

57. See BERMAN, *supra* note 14, at 9.

58. See *id.*; Kupetz, *supra* note 17, at 73.

59. See Kupetz, *supra* note 16, at 35.

60. See BERMAN, *supra* note 14, at 4.

proceeds thereof.⁶¹ Many states require the debtor to provide the assignee with a list of its shareholders and creditors and an inventory of its assets subject to the assignment.⁶² Whether these requirements are required by statute or just common law, all states require some form of notice.⁶³

These requirements give creditors a short time, anywhere from fifteen days to six months, to file a claim with the assignee.⁶⁴ As part of this notification process, the assignee is required to send “separate letters, by certified mail, to the IRS and all other appropriate taxing authorities, including taxing authorities in states, counties, and cities in which the debtor operated as well as the debtor’s state of incorporation.”⁶⁵ Once the assignee has taken these steps, he or she should begin figuring out precisely what assets are included in the assignment and how much is due to each creditor.⁶⁶

The assignee then conducts a winding down and/or liquidation or going-concern sale, and thereafter distributes the proceeds of the sale or liquidation to the debtor’s creditors.⁶⁷ The final step in the assignment process is either to request that the court close the estate, or in states where there is no court supervision, to provide notice to creditors that the estate is closed.⁶⁸ As in a federal bankruptcy proceeding, unsecured creditors have no right to pursue the assets assigned to the assignee.⁶⁹ Rather, these unsecured creditors are required to file a proof of claim to the assignee, and, if the claim is allowed, will ultimately participate in the assignee’s distribution of funds of the debtor’s estate.⁷⁰

61. *Id.* at 17.

62. *Id.*

63. *Id.*

64. *Id.*

65. *Id.* at 17–18.

66. *Id.* at 18.

67. See BERMAN, *supra* note 14, at 23–28; Kupetz, *supra* note 16, at 35. In the *ABCs of ABCs*, Berman discusses liquidation of assets, and how liquidation requires research and consultation with other professionals to figure out how the debtor’s assets could best be liquidated to maximize their value. There are a variety of ways that an assignee may conduct the liquidation; different assets can be liquidated in several ways, including a going-out-of-business sale, an auction of the assets either on a piecemeal basis or in bulk, a “negotiated” sale to a pre-arranged buyer, or a going-concern sale, with the assignee operating the business until the closing, in an effort to maximize the value of certain time-sensitive assets (i.e., supply contract) or to reduce exposure to contingent liability claims.

68. See BERMAN, *supra* note 14, at 52.

69. See BERMAN, *supra* note 14, at 5; Kupetz, *supra* note 16, at 34–35; Barr & Newman, *supra* note 35.

70. See Kupetz, *supra* note 16, at 34–35.

An ABC stops creditors from pursuing the debtor through collection lawsuits.⁷¹ The practical effect of many of the state laws surrounding ABCs is that these creditor actions are rendered ineffective.⁷² This does not mean, however, that creditors are left completely without a remedy.⁷³ Creditors can always file an involuntary bankruptcy petition without proof of the debtor's cash flow insolvency.⁷⁴ Proof of the ABC is itself grounds for involuntary bankruptcy relief.⁷⁵

Furthermore, choice of law bears significant import on the process of ABCs because it can complicate the process. The law of the state of the assignor's domicile, which in most cases is the law of the state where the assignment is made, generally governs ABCs.⁷⁶ The Restatement (Second) of Conflict of Laws proposes that the law of the state with the most significant relationship to the debtor and assignment should be applied, but acknowledges that this state will generally be the state of the assignor's domicile.⁷⁷ Many scholars suggest that if a company holds assets in multiple states, it should consolidate those assets into one state before beginning the ABC process in order to simplify the process.⁷⁸

ABCs will generally not be enforced when they conflict with the public policy of the state in which the assignment is sought.⁷⁹ Moreover, principles of comity do not require a state to give effect to an ABC brought in another state when doing so would "impair

71. BERMAN, *supra* note 14, at 4–5. Creditors are not completely powerless: they can challenge the validity of an assignment, and can also initiate involuntary bankruptcy proceedings. See Bruce C. Scalabrino, *Representing a Creditor in an Assignment for the Benefit of Creditors*, 92 ILL. B.J. 263, 265 (May 2004).

72. BERMAN, *supra* note 14, at 5.

73. See Davis, *supra* note 38, at 33; Richards & Ross, *supra* note 13, at 24 ("Subsequent voluntary or involuntary bankruptcy case can still take place. An ABC does not preclude the possibility of turning to bankruptcy later.").

74. Davis, *supra* note 38, at 33; Richards & Ross, *supra* note 13, at 24.

75. Richards & Ross, *supra* note 13, at 24.

76. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03; Judd v. J.W. Forsinger Co., 186 A. 525, 526–27 (N.J. 1936). When the debtor is a corporation, however, courts generally apply the corporate law of the state in which the debtor is incorporated; see also Maloy, *supra* note 52.

77. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

78. BERMAN, *supra* note 14, at 6; DEBTOR-CREDITOR LAW, *supra* note 29, § 35.07. As a side note, transferring assets to one state in order to consolidate jurisdiction should be okay, but there is still a risk of a creditor claiming fraudulent transfer and it should be considered. DEBTOR-CREDITOR LAW, *supra* note 29, § 35.10.

79. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

remedies or lessen security” of its own citizens.⁸⁰ Additionally, when a state has a statutory ABC system (as opposed to a common law ABC system), an ABC in that state will “only operate upon property in the jurisdiction in which the assignment is made.”⁸¹ As for property located in other jurisdictions, the law of that jurisdiction controls the rights of creditors generally.⁸²

C. How ABCs Fit into the Bigger Insolvency Picture: Comparing ABCs to Chapter 7 and Chapter 11 Bankruptcy

Businesses facing financial distress have several options available to them to address their financial issues beyond just ABCs.⁸³ ABCs vary from state to state, and Part III argues that one form of ABC is preferable over the other options, and thus reform should occur for ABC usage to become more frequent.⁸⁴ However, before it is possible to understand how one form of ABC can be preferable to another, it is necessary to compare ABCs to bankruptcy and explore how ABCs are both similar and different from bankruptcy.

Bankruptcy is a legal procedure for dealing with the debt problems of individuals and businesses, and is specifically filed under one of the chapters of title 11 of the United States Code.⁸⁵ United States bankruptcy courts are units of the federal district courts, and have jurisdiction over bankruptcy proceedings.⁸⁶ Businesses can file a voluntary case under either Chapter 11 or Chapter 7 of the Bankruptcy Code.⁸⁷ The federal nature of bankruptcy means that a bankruptcy case pending in one federal district is automatically enforceable throughout the country.⁸⁸ Thus, the automatic stay that applies in bankruptcy, whether a Chapter 11 or 7 case has

80. COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 15 (“This is due to the principle of comity, which does not require one state to give effect to an ABC in another state when doing so would impair remedies or lessen securities of its own citizens.”).

81. *Id.*

82. *Id.*

83. See JACK F. WILLIAMS, ASSIGNMENT FOR THE BENEFIT OF CREDITORS, STATE COURT RECEIVERSHIPS, AND BANKRUPTCY OPTIONS 3 (2009), available at <http://www.sbli-inc.org/archive/2009/documents/M.pdf>.

84. See *supra* Part III.

85. *Glossary*, U.S. COURTS, <http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Glossary.aspx> (last visited Mar. 29, 2014).

86. *Id.*

87. 11 U.S.C. §§ 701–84, 1101–74 (2012); see also *Bankruptcy: An Overview*, LEGAL INFO. INST., <http://www.law.cornell.edu/wex/bankruptcy> (last visited Apr. 15, 2014).

88. 28 U.S.C. § 1334(a) (2012).

commenced, applies on a national basis to protect the debtor's assets, "wherever located."⁸⁹

To understand how ABCs can better address a company's financial distress, it is first necessary to have a basic understanding of Chapter 11 and Chapter 7 bankruptcy cases and how they differ from ABCs.⁹⁰

1. Chapter 11 Bankruptcy

Chapter 11 of the U.S. Bankruptcy Code provides for a reorganization of the debtor, which may be in the form of either a rehabilitation of the debtor or an orderly liquidation.⁹¹ Sometimes distressed companies file for Chapter 11 bankruptcy specifically to sell "all or substantially all" of their assets using Section 363 of the Bankruptcy Code.⁹² Debtors frequently retain their assets and remain in business during the reorganization.⁹³ Generally, the debtor remains in control of the bankruptcy estate and proposes a plan of reorganization that sets a schedule of payments to creditors.⁹⁴ Ultimately, the debtor hopes that the court will confirm the plan so that the plan can be consummated.⁹⁵ Confirmed plans bind all the debtor's creditors, whether or not they have filed a claim and whether or not they have accepted the plan.⁹⁶

While Chapter 11 often resolves the financial problems of big corporations, small business Chapter 11 cases entail a less complex process than a full-blown Chapter 11 case.⁹⁷ Notwithstanding this

89. § 1334(e); *see also* 11 U.S.C. § 362(a) (2012).

90. Chapter 11 and Chapter 7 bankruptcies are complex matters with extensive case law and publications regarding them. This Note gives only a non-exhaustive description of Chapter 11 and Chapter 7 bankruptcies in the hope of illustrating that ABCs may be a viable alternative in some but not all cases. *See* COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 1; MARC BARRECCA & AMIT RANADE, *PICK YOUR POISON: ALTERNATIVE TO BUSINESS BANKRUPTCY 1* (2008), *available at* http://www.klgates.com/files/upload/barreca_pickyourpoison.pdf.

91. *See* WILLIAMS, *supra* note 83, at 5.

92. Justin K. Edelson & Christopher A. Ward, *Selling Distressed Assets: Weighing 363 Sales, Other Options*, TURNAROUND MGMT. ASS'N (Feb. 3, 2010), *available at* <http://www.turnaround.org/Publications/Articles.aspx?objectID=12351>.

93. *See* WILLIAMS, *supra* note 83, at 5.

94. *Id.*

95. *Id.* at 6 ("Plan confirmation can take two paths: (1) by unanimous consent or (2) by cram down so long as one non-insider impaired class of claim has accepted the plan.").

96. 11 U.S.C. § 1141(a) (2012).

97. *See* Davis, *supra* note 38, at 30. Under the U.S. Bankruptcy code, a "'small business case' means a case filed under chapter 11 of this title in which the debtor is a

streamlined process, small business Chapter 11 cases remain expensive.⁹⁸ Not every distressed company has the financial wherewithal to endure the time and costs associated with a Chapter 11 bankruptcy proceeding.⁹⁹ These expenses may be unjustified in simple cases or in cases involving small businesses.¹⁰⁰

Further, if the company is looking for a reorganization rather than a wind down or liquidation, a Chapter 11 bankruptcy proceeding would be preferable to an ABC.¹⁰¹ However, if the company does not have enough financing to continue operating throughout the bankruptcy process or if it is clear the company is going to close its doors, an ABC would be a more desirable process.¹⁰² In sum, in situations where there is insufficient cash to fund operations going forward, no significant revenues being generated, and gaining additional financing for the debtor seems unlikely, an ABC can be a better choice than a Chapter 11 case.¹⁰³

2. Chapter 7 Bankruptcy

ABCs are considered to be most similar to a Chapter 7 liquidation case.¹⁰⁴ A Chapter 7 bankruptcy case involves the liquidation of a

small business debtor.” 11 U.S.C. § 101(51C)–(51D) (2012). It further defines a small business debtor as:

[A] person engaged in commercial or business activities (including any affiliate of such person that is also a debtor under this title and excluding a person whose primary activity is the business of owning or operating real property or activities incidental thereto) that has aggregate non-contingent liquidated secured and unsecured debts as of the date of the filing of the petition or the date of the order for relief in an amount not more than \$2,000,000 (excluding debts owed to 1 or more affiliates or insiders) for a case in which the United States trustee has not appointed under section 1102 (a)(1) a committee of unsecured creditors or where the court has determined that the committee of unsecured creditors is not sufficiently active and representative to provide effective oversight of the debtor.

§ 101(51D).

98. See WILLIAMSON, *supra* note 4.

99. See Edelson & Ward, *supra* note 92.

100. See WILLIAMSON, *supra* note 4.

101. See Choslovsky & Walker, *supra* note 11, at 92. ABCs never rehabilitate a business; they end a business. In other words, if a business wants to go through bankruptcy in order to reorganize and attempt to stay in business, ABCs are not the right option.

102. COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 9; *Assignments for the Benefit of Creditors*, *supra* note 41.

103. Choslovsky & Walker, *supra* note 11, at 92; *Assignments for the Benefit of Creditors*, *supra* note 41.

104. See e.g., BERMAN, *supra* note 14, at 3; DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03; WILLIAMSON, *supra* note 4; Choslovsky & Walker, *supra* note 11, at 91.

debtor's assets.¹⁰⁵ In Chapter 7 bankruptcy, a trustee in bankruptcy generally identifies, collects, liquidates, and distributes all of the debtor's assets.¹⁰⁶ While individual debtors receive a discharge from most unsecured obligations that remain unpaid at the conclusion of a Chapter 7 case, corporate debtors do not.¹⁰⁷

Chapter 7 trustees are often lawyers or accountants, who are assigned cases in large numbers; their task is to efficiently analyze whether the business has any assets that can be readily liquidated for cash.¹⁰⁸ They may have no experience in the particular industry of the company or in running businesses at all.¹⁰⁹ In an ABC, on the other hand, the debtor can select an assignee with appropriate experience and expertise to conduct the "wind down of its business and liquidation to its assets."¹¹⁰

Further, in a Chapter 7 case, the business's directors and owners are excluded from the liquidation process.¹¹¹ A trustee in bankruptcy supersedes their authority.¹¹² In most states' ABCs, however, these principals may participate to whatever extent they choose to, as long as they have not engaged in illegal or improper conduct.¹¹³

In Chapter 7, debtors must file numerous forms with the court.¹¹⁴ In ABCs, whether forms need to be filed with the court and the amount of court involvement depend on the state.¹¹⁵ Generally, however, in states where common law ABCs are used, no formal filing is required prior to the occurrence of the assignment.¹¹⁶

105. WILLIAMS, *supra* note 83, at 3.

106. *Id.* at 4.

107. 11 U.S.C. § 727(a)(1) (2012). Thus, an ABC's lack of discharge is not a basis for distinguishing between bankruptcy and these state law remedies.

108. Davis, *supra* note 38, at 26.

109. *Id.*

110. *See* Kupetz, *supra* note 16, at 36.

111. 11 U.S.C. §§ 701, 704 (2012). The Court appoints an impartial case trustee to administer the case and liquidate the debtor's nonexempt assets.

112. *Id.* § 721 (Authority to operate business); *id.* § 783 (Additional powers of the trustee).

113. *See* Davis, *supra* note 38, at 27–28.

114. § 704; U.S. COURTS, *United States Bankruptcy Court Required Lists, Schedules, Statements and Fees*, U.S. COURTS, http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/BK_Forms_Current/B_200.pdf (last visited Apr. 15, 2014) [hereinafter *U.S. Bankruptcy Courts Lists*].

115. *See infra* Part III.

116. *See infra* Part III.A.

3. *Advantages of ABCs over Federal Bankruptcy*

Overall, compared to Chapter 11 and Chapter 7 bankruptcy, ABCs are considered to be less time consuming, less expensive, less public, and less subject to oversight.¹¹⁷ ABCs are also viewed to be faster and to contain more flexibility due to the lack of cumbersome procedural requirements.¹¹⁸ For example, Chapter 7 and Chapter 11 bankruptcies have more paperwork and judicial involvement,¹¹⁹ whereas ABCs, depending on the state, generally are less formal and require less documentation.¹²⁰

ABCs also require less work for the board of directors and management than a Chapter 11 case because the assignee handles operations through the end of the assignment.¹²¹ On the other hand, in a reorganization case, managers and directors are often responsible for winding down business and disposing of the assets.¹²² Further, even when a trustee is appointed in a Chapter 7 liquidation case, the assignee in an ABC is often preferable because the company can

117. Choslovsky & Walker, *supra* note 11, at 91.

118. James A. Chatz & Joy E. Levy, *Alternatives to Bankruptcy*, 17 NORTON J. BANKR. L. & PRAC. 149, 153 (2008) (“An assignment is often less expensive than a Chapter 11. Additionally, an ABC provides greater flexibility than would be available in a Chapter 7 or 11 bankruptcy proceeding.”).

119. 11 U.S.C. §§ 521, 704, 1106 (2012); *U.S. Bankruptcy Courts Lists*, *supra* note 114.

120. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

121. *Cf.* Jay Alix et. al., *Assignments for the Benefit of Creditors*, in FIN. HANDBOOK BANKR. PROF. § 3.14 (2d ed., 2013) (“The assignee takes possession of the debtor’s premises directly, or delegates physical possession to a custodian. Locks are changed, notice of Assignment is posted on the door of the business, and full security measures are implemented.”); Kupetz, *supra* note 17, at 73.

122. *See* CAROLINE FULLER & GEOFFREY L. BERMAN, *BANKRUPTCY V. RECEIVERSHIP V. ASSIGNMENT FOR THE BENEFIT OF CREDITORS: ADVANTAGES AND DISADVANTAGES OF EACH* (2009), available at <http://www.abiworld.org/committees/newsletters/busreorg/vol8num8/comparative.pdf>. In Chapter 7 bankruptcy, the trustee typically never operates the business although they make seek court approval to have interim authority to do so. *See id.* In Chapter 11 bankruptcy, the managers and directors maintain authority to operate company in ordinary course of business, and the management is paid in the ordinary course of business. *See id.* However, in both ABCs and bankruptcy, the fiduciary duty that managers and directors owe to their company extends to creditors once their company enters the zone of insolvency. *See* Jeffrey Baddeley, *Defending Directors and Officers Against Breach of Fiduciary Claims in Bankruptcy*, BLOOMBERG BNA (Sept. 27, 2012), available at <http://about.bloomberglaw.com/practitioner-contributions/defending-directors-and-officers-against-breach-of-fiduciary-duty-claims-in-bankruptcy>. *But see* COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 9 (explaining that ABCs differ from bankruptcy in that “ABCs typically require that an officer of the company has to ‘stay on board’ to ensure the ABC is properly executed and carried through.”).

select someone with expertise in marketing and selling assets in that particular industry as the assignee.¹²³ Since the assignee has experience operating a business, he or she will operate the business of the insolvent company as long as need be to maximize return by realizing some form of going concern value.¹²⁴ They are also experts at convincing creditors to be patient.¹²⁵

Furthermore, ABCs generally generate less negative publicity, if any publicity, whereas bankruptcy is public and can reflect negatively on the company.¹²⁶ For example, in bankruptcy, the headline might read “Company shuts its doors” or “Company files for Bankruptcy,” but with an ABC, by the time news reaches the media, the headline will read “New Company Acquires Old One.”¹²⁷

4. *Disadvantages of ABCs over Bankruptcy*

While there are many advantages of ABCs, there are still some disadvantages in choosing an ABC over a bankruptcy proceeding.¹²⁸ ABCs are not and never should be a default answer for how to deal with any insolvent company. First, ABCs “[lack] the institutional formality and widespread familiarity of a formal bankruptcy proceeding” because they are infrequently used.¹²⁹ Additionally, it can be difficult to find buyers in ABCs because some buyers may refuse to purchase assets outside of a Chapter 11 or Chapter 7 bankruptcy, which provides statutory protections to buyers.¹³⁰ Often, specifically in states where the ABC process is non-judicial, there is no court order approving the sale by the assignee.¹³¹ Some buyers prefer the clarity given by those court orders, so they will stay away from purchasing assets from an ABC.¹³² Further, in an ABC, an assignee may not sell property free and clear of liens,¹³³ and executory

123. See BERMAN, *supra* note 14, at 9; Edelson & Ward, *supra* note 92.

124. See Davis, *supra* note 38, at 27–28.

125. *Id.*

126. See Kupetz, *supra* note 16, at 36.

127. See *id.*; Kupetz, *supra* note 17, at 73.

128. This is not an exhaustive list of the disadvantages but rather a brief list meant to show that there are advantages and disadvantages to using ABCs over bankruptcy.

129. See COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 16.

130. 11 U.S.C. § 363(f) (2012) (discussing the circumstances in which a trustee may sell certain property free and clear of any interest in such property). See generally § 363; *Assignments for the Benefit of Creditors*, *supra* note 41.

131. See Kupetz, *supra* note 16, at 36.

132. *Id.*

133. See WILLIAMS, *supra* note 83, at 9; Kupetz, *supra* note 16, at 36. In bankruptcy, on the other hand, a trustee may sell certain property free and clear of

contracts and leases cannot be assigned without the consent of the other party to the contract.¹³⁴ In ABCs, the debtor's debts are not discharged,¹³⁵ and there is limited or no immunity provided to assignees.¹³⁶ There is also no automatic stay in ABCs, as there is in bankruptcy.¹³⁷ Additionally, the preference power does not exist in most states and is controversial in those states that do recognize it.¹³⁸ Further, as mentioned above, there is limited territorial jurisdiction for ABCs, so companies often must consolidate their assets in one state before performing an ABC.¹³⁹ Bankruptcy, on the other hand, is a matter of exclusive federal jurisdiction; thus, there is no need to consolidate assets or worry about the differing laws between states.¹⁴⁰

Finally, the debtor company's owner may have personally guaranteed the company's debts, in which case both Chapter 7 and Chapter 11 bankruptcies might present enormous efficiency.¹⁴¹ As mentioned previously, ABCs do not provide a discharge of the business's debts.¹⁴² While a corporation similarly does not receive a discharge at the conclusion of a Chapter 7 bankruptcy case,¹⁴³ many banks require the owner of a small business organized as a corporate entity to guarantee the lending obligations of the owner's business. As a result, individual owners of an insolvent corporation may themselves require the protections of a bankruptcy filing in order to

any interest in such property subject to certain exceptions set forth in 11 U.S.C. § 363(f).

134. See § 365 (discussing executory contracts and unexpired leases in the bankruptcy context); Kupetz, *supra* note 16, at 36.

135. For businesses, the lack of discharge is no disadvantage compared to Chapter 7 bankruptcy because it only offers discharge to individuals. See 11 U.S.C. § 727 (2012); see also Davis, *supra* note 38, at 33 ("Because modern assignments for the benefit of creditors still do not provide a discharge of the assignor's debts, individuals and partnerships generally do not utilize them. Individuals and individual partners must look to bankruptcy law for a discharge.").

136. See 11 U.S.C. § 704 (2012) (duties and immunities of Chapter 7 trustee); *id.* § 1106 (duties and immunities of Chapter 11 trustee); WILLIAMS, *supra* note 83, at 9.

137. Eisenbach, *supra* note 9; 11 U.S.C. § 362 (automatic stay in bankruptcy).

138. See WILLIAMS, *supra* note 83, at 9. For more information on the problems state preference statutes have encountered, see Luo, *supra* note 15. For preferences in bankruptcy, see 11 U.S.C. § 547 (2012).

139. See WILLIAMS, *supra* note 83, at 9; *supra* Part I.B.

140. See 28 U.S.C. § 1334 (2012); COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 16; WILLIAMS, *supra* note 83, at 9.

141. ABCs do not deal whatsoever with guarantees. Thus, if the debtor made a guarantee, the trustee has to figure out a way around it, which can significantly reduce the efficiency of ABCs.

142. See *supra* note 106 and accompanying text.

143. 11 U.S.C. § 727(a)(1) (2012) ("The Court shall grant the debtor a discharge, unless the debtor is not an individual.").

receive a discharge from the guarantee obligation; in some instances, there may be strategic advantages to simultaneous filing of related corporate and individual bankruptcy cases, but these synergies vary from case to case and should not be presumed.¹⁴⁴

D. A Brief History of ABCs and Their Reform

ABCs originated at common law, where they functioned as liquidation procedures for troubled debtors, just as they do today.¹⁴⁵ Although Congress passed federal bankruptcy laws, ABCs have persisted, evolved with the times, and remain a viable alternative¹⁴⁶ to formal bankruptcy proceedings.¹⁴⁷ Although ABCs have been used frequently in recent years in states such as California, Illinois, and Florida, “there are relatively few reported cases discussing ABCs and even fewer modern cases.”¹⁴⁸

Nevertheless, ABCs are not an antiquated legal concept. Not only have they found use in several states in recent years, but they also greatly resemble similar “winding up” procedures used frequently throughout Europe and Australia.¹⁴⁹ Further, the call to reform ABC procedures is not a new one.¹⁵⁰

144. David M. Madden, *Dissecting Chapter 7 Bankruptcy for Businesses*, J. DUPage COUNTY B. ASS'N (2009), <http://www.dcbabrief.org/vol220510art4.html> (“A business Chapter 7 will not stop a creditor from pursuing a shareholder in connection with the shareholder’s personal guaranty of a business line of credit or preclude an action for the liability associated with the business’s debts. As such, individuals facing personal liability for substantial business debt often consider filing for personal bankruptcy in coordination with the business bankruptcy, in order to eliminate personal liability for the business debt.”).

145. See, e.g., BERMAN, *supra* note 14, at 1; DEBTOR-CREDITOR LAW, *supra* note 29, § 35.02; Choslovsky & Walker, *supra* note 11, at 91.

146. When Congress first created a uniform bankruptcy law, exercising its constitutional powers to do so under Article 1, Section 8(4) of the Constitution, the Supreme Court was faced with the question of whether ABC’s would continue to be a viable alternative state regime for business liquidation, and the court answered in the affirmative. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.02; Choslovsky & Walker, *supra* note 11, at 92.

147. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.01.

148. *Id.*

149. *An Out-of-Court “Winding Up” Entitled to Recognition Under Chapter 15? You Bet!*, SOUTHBAY L. FIRM BLOG (Mar. 23, 2009, 6:46 P.M.), <http://www.southbaylawfirm.com/blog/?p=141> (“A voluntary ‘winding up’ is essentially a private liquidation authorized by the Australian Corporations Act, conducted by company-retained liquidators under the auspices of the Australian Securities & Investments Commission (ASIC) and reviewable on appeal by Australian courts. It has statutory analogues in most countries whose civil law derives from the old British Commonwealth system, and is very generally analogous to an American ‘assignment for the benefit of creditors’ (ABC). ABCs are recognized under the laws of virtually every state in the US, and—in California—are

This Note offers a fresh take on how states can reform their ABC processes to make ABCs more accessible, maximize their benefits, and more frequently use them. Many times in the history of ABCs, advocates of ABCs have recognized that ABCs were becoming too “particularized to fit the needs of those states that have found the process a useful tool.”¹⁵¹ As a result, ABCs were so diverse that “[they] were less useful than [they] might otherwise be because of the significant differences among state laws governing the process.”¹⁵²

In the 1990s, the American Bankruptcy Institute proposed the adoption of “statutes that would make the state laws on general assignments more uniform, and hopefully more utilized on a national basis.”¹⁵³ While practitioners throughout the country considered these proposals, the issue was dropped until recently when practitioners began again to advocate for reform.¹⁵⁴ In response, additional statutory reforms, including a Model Statute on General Assignments, were suggested.¹⁵⁵

In drafting a model statute, these advocates proposed having bonds to be posted by the assignee at the time of the assignment, requiring “consent” to the assignment by a majority of the creditors, and having court supervision.¹⁵⁶ However, the model statute raised as many questions as it solved by incorporating comments within its text about items that would need to be later resolved.¹⁵⁷ For example, while the model statute referred to posting bonds, it contained no bond requirement.¹⁵⁸ Further, within its text, the model statute conceded that involuntary bankruptcy may be preferable to creditors, suggesting the writers of the model statute did not themselves believe in the strength of ABCs as a preferable alternative to bankruptcy.¹⁵⁹ Likely due to these flaws, no state has yet adopted the model statute,

commonly used as a very quick and inexpensive means of winding up a company’s affairs and disposing of its assets.”).

150. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.02; Choslovsky & Walker, *supra* note 11, at 92.

151. See Berman & Vance, *supra* note 27, at 33.

152. *Id.*

153. *Id.*

154. *Id.*

155. *Id.* at 34.

156. *Id.* at 35.

157. *Id.* at 35 n.4.

158. *Id.* at 44.

159. See *id.* (“The remedy of an involuntary bankruptcy petition may be more appropriate for creditors.”).

but should any model statute be drafted in the future, it should consider the issues described below.

II. A SPECTRUM OF ABCs AND COMPARING THE VARIOUS FORMS ACROSS THE STATES

ABCs are used frequently in some states, such as California, Florida, and Illinois, and infrequently or rarely in other states despite their being an attractive alternative¹⁶⁰ in certain situations.¹⁶¹ Today, some states maintain tight control over the ABC process while others provide little regulation.¹⁶²

This state-to-state variance in ABC procedure has led some scholars to conclude that there are two approaches to the assignment process¹⁶³ and others to describe ABCs as existing in three forms.¹⁶⁴ This Note argues that ABCs are best explained as existing on a spectrum from one pole that is purely common law, to another pole in which ABCs are heavily regulated and lose most of their advantages over formal bankruptcy proceedings.¹⁶⁵ For the purposes of explaining the ABC processes without examining each states ABC individually, the following sub-Parts break ABCs in three categories: states with common law ABCs, states with minimally regulated ABCs, and states with heavily regulated ABCs.¹⁶⁶

Recognizably, the success of an ABC depends on maximizing its benefits over bankruptcy by being more flexible and thrifty; frequency of its use depends on practitioners' familiarity with its state's ABC process. There are positive and negative aspects, however, within each category. This Part examines each category of

160. *See infra* Part II.C.

161. Richards & Ross, *supra* note 13, at 5.

162. Blakely, *supra* note 50, at 1.

163. *See* BERMAN, *supra* note 14, at 3 (“[O]ne approach requires court supervision of the assignment and the assignee; the other permits assignments to proceed without court supervision, but requires that the assignee follow state laws applicable to and governing the liquidation of a business and its assets.”).

164. Richards & Ross, *supra* note 13, at 7 (describing ABCs as existing in three forms which are minimalist states, states with a medium amount of requirements, and states with the widest scope of statutory requirements).

165. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03. Although it would seem only logical that the statutes most frequently used would fall somewhere within this spectrum, after analyzing the ABC process of the states where they are most frequently used, there appears to be no correlation between how regulated the ABC process is and the frequency of its use. *See infra* Part II A–C.

166. Richards & Ross, *supra* note 13, at 7 (describing ABCs as existing in three forms which are minimalist states, states with a medium amount of requirements, and states with the widest scope of statutory requirements).

ABCs to determine which is preferable and which parts of each should be used to create a new category. Thus, this Note evaluates the advantages and disadvantages of the processes found within the spectrum in order to uncover the form of ABC that would be most useful.¹⁶⁷

A. States with Common Law ABCs

Although some form of ABC exists in all states, only thirty-three states have statutes governing ABCs, to varying degrees. Until the 1900s, practically all ABCs involved common law assignments.¹⁶⁸ While most states have enacted statutory schemes of ABCs, some still depend on common law to regulate these assignments.¹⁶⁹ Today, ABCs are governed by common law in eleven states, including Illinois and Hawaii.¹⁷⁰ A common law ABC involves no comprehensive statute governing the creation, validity, or administration of ABCs.¹⁷¹

In its common law form, the ABC process is relatively uncomplicated because the process usually does not require any filings or court approval.¹⁷² Because a common law ABC is usually an out-of-court process, many courts will only see ABCs in these states when and if disputes occur.¹⁷³ Common law ABCs begin when the debtor executes a deed of assignment of all assets to an assignee who then becomes a fiduciary for the creditors.¹⁷⁴ Once the assignment has occurred and the assignee has taken inventory of the assets and the creditor's claims, the assignee liquidates the assigned assets and makes a pro rata distribution to the creditors who filed claims with the assignee.¹⁷⁵ Common law ABCs thus give the debtor enormous flexibility in setting the terms and conditions of the assignment.¹⁷⁶

167. This section will treat ABCs as if there are three types of ABC processes: (1) the predominantly common law ABC, (2) the moderately regulated statutory ABC, and (3) the heavily regulated ABC. Granted, each state's statute may fall in between these three extremes but overall these three categories encompass the three types of that ABCs take amongst the states. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03 (discussing statutes that require court involvement such as the filing of documents with the court and supervision of the court); *infra* Part II.C.

168. DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

169. *See* Luo, *supra* note 15, at 523.

170. *See* DEBTOR-CREDITOR LAW, *supra* note 29, at § 35.03.

171. *See* Verbrugge, *supra* note 30, at 1.

172. *Id.*

173. *See* DEBTOR-CREDITOR LAW, *supra* note 29, at § 35.03.

174. *See* Verbrugge, *supra* note 30, at 1.

175. *Id.*

176. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.02.

Common law ABCs are admittedly hard to summarize, because there are no comparable statutes and each state's case law differs from other states' case law. Further, usually in common law ABCs, the instrument of the assignment, or the agreement entered into by the parties to the assignments, defines the powers and duties of the trustee and the manner of distribution.¹⁷⁷ To illustrate how common law ABCs differ, this Part examines the case law in a state in which a common law ABC is frequently used, Illinois, and that of a state whose common law ABC is infrequently used, Hawaii.

The Illinois ABC is so popular that some scholars have concluded that debtors in financial distress are as likely to rely on it as on federal bankruptcy law in Illinois.¹⁷⁸ In Illinois, since ABCs are out-of-court remedies, the assignee is not even required to seek creditor or court approval for administration of the estate.¹⁷⁹ Illinois courts consider an ABC to be a unique trust arrangement whereby the assignee holds the property for the benefit of a special group of beneficiaries consisting of the assignor's creditors, and when the time is right, liquidates it in order to use the proceeds of the assets as payments to the creditor.¹⁸⁰

Although an Illinois ABC is not statutorily regulated and does not have any consent or approval requirements, there are still certain formalities that Illinois ABCs must meet.¹⁸¹ First, the debtor and assignee must create a written instrument detailing the powers of the assignee over the trust.¹⁸² Without this formal written agreement, courts will invalidate an attempted ABC that gets challenged.¹⁸³ While the lack of a formal written agreement will invalidate an attempted ABC, it will not deprive any creditor of its rights.¹⁸⁴ Rather, the effect of failing to make a formal written agreement is that the debtor's property remains in the debtor's property as if no ABC had been attempted.¹⁸⁵

Although Hawaii's ABC is rarely used, it differs in important ways from the Illinois ABC. For example, while Hawaii's ABC is a common law ABC, Hawaii's Fraudulent Transfer Law heavily

177. See Russell J. Davis et. al., *Creditors' Rights § 34: Common-law and Statutory Assignments Compared*, 23 OHIO JUR. 3D (2013).

178. Morrison, *supra* note 11, at 257.

179. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

180. *Id.*

181. *Id.*

182. *Id.*

183. *Id.*

184. *Id.*

185. *Id.*

impacts how its ABC process is conducted, causing Hawaii's ABC process to be impacted, at least to some extent, by statutes.¹⁸⁶ Further, while the Illinois legislature seems to believe that ABCs are best left as they are, Hawaii's legislature has proposed reforming Hawaii's ABC process to make it statutorily regulated, although to date these proposals have not been adopted.¹⁸⁷ If passed, Hawaii would require the assignee to sign acceptance of the assignment and to file the assignment with the clerk of the state circuit court.¹⁸⁸ This bill would give courts control over the ABC process, not just disputes arising in that context.¹⁸⁹ The purpose of these revisions is to eliminate priority disputes that sometimes occur in the wake of a completed ABC,¹⁹⁰ but nonetheless would subject Hawaiian ABCs to heightened administrative cost and expense.

Although common law ABCs can be efficient, flexible and cost saving, they also have drawbacks. In the absence of formal legislative requirements, the instrument of the assignment usually defines the powers and duties of the trustee and the manner of distribution.¹⁹¹ Thus, practitioners must either have extensive knowledge of how to conduct an ABC in that state, or research the case law surrounding ABCs in that jurisdiction before they can conduct the assignment.¹⁹² Case law can be voluminous and, in any event, can provide less guidance than a statute. This may either dissuade practitioners from pursuing ABCs as an option or it will cause billable hours to stack up and thus add additional administrative costs that detract from the cost-saving abilities of ABCs.

Further, common law ABCs lack judicial review prior to the completion of the ABC process.¹⁹³ Courts can impose restrictions after the assignment and subsequent liquidation has occurred, but cannot oversee the process or require filings until after litigation is

186. See Verbrugge, *supra* note 30, at 2 ("If a creditor is able to establish that the assignment violates HAW. REV. STAT. § 651 C-4 or HAW. REV. STAT. § 651 C-5, then the creditor would be able to have the transfer avoided under HAW. REV. STAT. § 651C-7.").

187. *Id.* at 1.

188. *Id.* at 12.

189. *Id.*

190. *Id.*

191. See Davis, *supra* note 177, at 14.

192. Cf. Verbrugge, *supra* note 30, at 1 (arguing that statutes can help to clarify a state's common law concerning the "creation, validity, and administration of an assignment for the benefit of creditors").

193. See Scalabrino, *supra* note 71, at 264; cf. Choslovsky & Walker, *supra* note 11, at 93.

brought.¹⁹⁴ As a result, courts cannot prevent problems in this context; they only react to them.

There is also less transparency in common law ABCs because there may be no requirement that creditors receive notice, and in some places, a common law ABC can occur without prior notice to all shareholders or creditors.¹⁹⁵ There may be factual disputes regarding when the assignment was made and if sufficient notice was given to creditors, but without transparency, filings, or certain other requirements, it is often difficult to tell when exactly an assignment was made.¹⁹⁶ Finally, the flexibility of common law ABCs has a large potential for abuse because they give the debtor a wide berth of freedom and give creditors almost no control over the assignee.¹⁹⁷ For these reasons, many prefer ABCs in which statutes govern the process.¹⁹⁸

B. States with Minimally Regulated ABC Processes

ABC statutes either supplement common law ABCs or override them.¹⁹⁹ In some states, ABC statutes are permissive, allowing common law ABCs to continue alongside their statutory counterpart, essentially codifying the common law format.²⁰⁰ Generally, ABC statutes that are designed to supplement the common law fall into the minimally regulated statutory ABC category, which some might call a

194. Depending on how you view the court's oversight abilities in ABCs, this can either be a major drawback or a major advantage. *Compare* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03 (arguing that less court involvement saved time and made the ABC more efficient), *with* Verbrugge, *supra* note 30, at 135 (noting that court supervision can help reduce or eliminate factual disputes related to the assignment).

195. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03; Verbrugge, *supra* note 30, at 135.

196. *Cf.* Verbrugge, *supra* note 30, at 1. As is, Hawaii currently has no set notice requirements, and the deed of assignment currently sets notice requirements on a case-by-case basis. Further, because the express consent of creditors is not a necessary element of an ABC in Hawaii, an ABC could occur without a creditor even being aware of the assignment.

197. *Id.*; *see* Mann, *supra* note 22, at 1394 (calling the ABC process a very secret process and saying, "The basic point is that the process can be accomplished quickly, without a public filing, and often without any public notoriety.").

198. *See* Edelson & Ward, *supra* note 92, at 6 ("An ABC is a particularly attractive option in Delaware because the state is one of the few in which statutes govern the process rather than relying solely on common law."); Verbrugge, *supra* note 30, at 8.

199. *See* Chatz & Levy, *supra* note 118, at 153 (noting various state statutes merely codify the common law concept or essentially override it).

200. Choslovsky & Walker, *supra* note 11, at 91.

mix between statutory and common law ABCs.²⁰¹ In other words, minimally regulated ABCs involve the middle ground between common law ABCs and heavily regulated ABCs, and thus exist across a wide spectrum.

For the purposes of this Note, the spectrum of minimally regulated ABCs begins where common law ABCs end. This category covers ABC statutes that are extremely brief and do little more than refer to judicial decisions—for example, Iowa’s statute—all the way to ABC statutes that involve the judiciary by requiring assignees to merely file notice of the assignment with the court.²⁰²

The most famous minimally regulated ABC is arguably California’s because it is used more frequently than any other state’s ABC.²⁰³ Dot-com companies and private equity and venture capital companies frequently rely on the California ABC format.²⁰⁴ The California common law ABC was absorbed into California state law governing an ABC, but over time, the California legislature repealed the complete absorption and eventually returned to a predominantly common law ABC system.²⁰⁵ They enacted “supplementary statutes,” however, to address specifically troubling aspects of ABCs.²⁰⁶ These supplementary statutes contain very bare bones requirements, and even with them, California does not require a public court filing and the debtor’s assigned assets can be sold without court approval.²⁰⁷ Among the rules enacted by the supplementary statutes is a notice rule requiring the assignee to set a deadline and give 150 to 180 days’ notice to creditors of the assignment for submission of claims to the assignee.²⁰⁸ California also requires debtors to provide the assignee with a list of creditors, shareholders, and other parties in interest.²⁰⁹ Further, California has a complex priority scheme that includes giving priorities for unsecured claims for up to \$4,300 for each individual,

201. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03 (describing this category as a mix between statutory and common law).

202. *Id.*; see, e.g., IDAHO CODE ANN. § 68-201 (2006).

203. See COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 12; DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03; Luo, *supra* note 15, at 513; Mann, *supra* note 22, at 1390.

204. See COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 12; *supra* Introduction, Parts I, II.

205. See Luo, *supra* note 15, at 524.

206. See *id.*; Eisenbach, *supra* note 9. Examples of “troubling aspects” include the time allowed for notice to be given and the required components of notice to creditors.

207. Eisenbach, *supra* note 9, at 2.

208. CAL. CIV. PROC. CODE § 1802 (West 1992).

209. *Id.*

priority for consumer deposit claims, and priority treatment of claims for wages, salaries, commissions, and employee benefit contributions.²¹⁰

The drawbacks of minimally regulated statutes are hard to pin down because they fall across such a wide spectrum. In states where no court filing is necessary, one drawback at least from the standpoint of analyzing ABCs and their impact, is that no statistics are kept.²¹¹ In states where filing after the fact is required or a certain date is tracked by the state, statistics on filings are generally kept in the offices of city and county clerks.²¹² Regardless, it is very difficult to get an aggregate number about how many ABCs occur statewide in states with minimally regulated ABCs.²¹³ This also makes it more challenging to study the effects of these types of ABCs.²¹⁴ Without more knowledge, it is difficult to encourage other states to reform their ABCs to adopt a process about which there is very little empirical data.

Another drawback is that many minimally regulated ABC statutes, such as California, do not give rise to an automatic stay, as in bankruptcy.²¹⁵ The lack of a stay means that creditors can obtain judgments in pending lawsuits, which effectively could help some creditors jump the line of all creditors and collect on these judgments ahead of the line.²¹⁶

210. *Id.* § 1204(a) (1999). In *Sherwood Partners v. Lycos Inc.*, the Ninth Circuit struck down California's preference law, which allowed assignees for the benefit of creditors to avoid preferential transfers to creditors. See 394 F.3d 1198 (9th Cir. 2005), *cert. denied*, 546 U.S. 927 (2005). Despite their invalidation of the law, many still argue that preference actions are still good law. See Geoffrey L. Berman & Catherine E. Vance, *State Law Preference Actions: Still Alive after Sherwood Partners v. Lycos*, 26 AM. BANKR. INST. J. 24, 24 (2008); David S. Kupetz, *The Venerable Assignment for the Benefit of Creditors Weathers the Ninth Circuit's Decision in Sherwood v. Lycos and Remains a Valid Alternative to Federal Bankruptcy Proceedings*, 2008 ANN. SURVEY BANKR. L. 12; Luo, *supra* note 15, at 513.

211. See Mann, *supra* note 22, at 1394. Although this is listed as a disadvantage for minimally regulated ABCs, it is a disadvantage that flows across the entire spectrum of ABCs. Empirical data on ABCs is very difficult to find, and where it can be found, it is hard to compare it to any other states since data is sparsely collected.

212. *Id.* at 1394–96.

213. *Id.*

214. *Id.*

215. See Luo, *supra* note 15, at 522; Eisenbach, *supra* note 9, at 2.

216. See Luo, *supra* note 15, at 522.

C. States with Heavily Regulated ABC Forms

In addition to minimally regulated ABCs and common law ABCs,²¹⁷ there is a third category of ABCs: the heavily regulated ABC. Heavily regulated ABC statutes essentially abolish the common law form and create a new, separate ABC process.²¹⁸ There is some variation, however, even between different states' heavily regulated ABCs.²¹⁹ For example, while some ABC statutes may not expressly render common law ABCs void, others do.²²⁰

Whether the statutes explicitly or implicitly override common law ABCs, all such statutes govern the procedural formalities associated with this process, including "whether they must be recorded, when the assignee must give notice to creditors, whether the assignee must be bonded, the nature of the schedule of assets and liabilities that the assignee must file with the court, and court supervision of the proceedings."²²¹ They also make explicit who is authorized to make these assignments, the requisites for a valid assignment, the role and duties of an assignee, how an assigned estate is to be managed and administered, and the manner in which creditors' claims are to be presented, proved, and paid.²²²

In heavily regulated ABCs, courts often oversee the entire process, imposing duties that range from approving the assignee to filing interim reports with the court.²²³ For example, in Ohio, an assignee is required to file a verified inventory of all estate property with the court; in New York, the assignee is required to file multiple times with the court, including a final report in connection with the termination of the trust.²²⁴ In Delaware, the Court of Chancery is very involved in the proceedings, which some practitioners see as an unmitigated positive, given the court's prestige.²²⁵

217. See *supra* Part II.A–B.

218. See Chatz & Levy, *supra* note 118, at 153 (discussing how "some states effectively abolish common law ABCs by requiring that all ABCs be made in accordance with those statutes"); Choslovsky & Walker, *supra* note 11, at 91.

219. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

220. *Id.* (discussing how Michigan's ABC statute preempted the common law ABC).

221. See Chatz & Levy, *supra* note 118, at 153.

222. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

223. See, e.g., COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 13; DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03; Barr & Newman, *supra* note 35, at 11.

224. Barr & Newman, *supra* note 35, at 10. These mirror similar obligations under bankruptcy law.

225. See COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 13; Edelson & Ward, *supra* note 92. Notably, there is a big difference between

Florida has a heavily regulated ABC process that is a popular alternative to bankruptcy and has seen frequent use amongst in-state insolvent companies.²²⁶ In recent years, reform was initiated in Florida to create an ABC statute that would provide a “uniform procedure for the administration of insolvent estates and to ensure full reporting to creditors and equal distribution of assets according to the Florida ABC statute.”²²⁷ Many believe Florida’s amended ABC statute “substantially reduces the number of situations in which the advantages of bankruptcy outweigh those of an ABC.”²²⁸ Furthermore, scholars believe that having a uniform ABC procedure will enable more practitioners to understand and use ABCs in the future.²²⁹

In Florida, the ABC process commences when the debtor and the assignee enter into an irrevocable assignment.²³⁰ The debtor is required by law to assist the assignor with the process.²³¹ The debtor also must submit him or herself to an under-oath examination by the assignee about all acts, conduct, assets, liabilities, his or her financial condition, and any other matters related to the assignee’s administration of the estate.²³² The assignee then files a petition in state court, to which the assignment document, along with the schedules of assets and creditors, are attached.²³³ The ABC proceeds as an ongoing case, which simplifies the process of obtaining court assistance. Thus, like in other cases, court authorizations, approvals of transactions, determinations of bond amounts, orders of cooperation of third parties, and resolutions of disputes are initiated by motion.²³⁴ This differs from ABCs in other states where to obtain court assistance, one has to initiate a motion.²³⁵ The assignee must also create a register of all claims filed against the estate and make it

having access to that court if creditors see a problem with the process, and having to report to the court along the way, which may just increase the cost of the proceeding and thus dilute the advantages of using an ABC over bankruptcy.

226. See DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03; Davis, *supra* note 38, at 33.

227. See DEBTOR-CREDITOR LAW, *supra* note 29, at § 35.03; Ronald G. Neiworth & Jason Bloom, *Florida Legislature Overhauls Assignment for the Benefit of Creditors*, 82 FLA. B.J. 21, 21 n.3 (2008).

228. See Davis, *supra* note 38, at 18.

229. See Neiworth & Bloom, *supra* note 227.

230. FLA. STAT. § 727.104(1)(b) (2007).

231. *Id.* § 727.107(3).

232. *Id.*

233. *Id.*

234. See Davis, *supra* note 38, at 19–20.

235. *Id.* at 20.

available to all creditors, who can then review and challenge any of those claims.²³⁶

Florida, like many other states with heavily regulated ABCs, limits an assignee's ability to run the debtor's business.²³⁷ In the past, Florida required court authorization for the assignee to run the debtor's business.²³⁸ Today, however, if it is in the estate's best interest, Florida allows the assignee to conduct the assignor's business without court approval, for at least fourteen days and for up to a total of forty-five days upon notice.²³⁹ After forty-five days, court authorization is required.²⁴⁰ This important change permits a "seamless transition in operation" from the debtor to the assignee, and enables the assignee to sell off the assets of the business more easily.²⁴¹ Court approval is still required for selling off the assets.²⁴²

Extensive and detailed procedures for the administration of ABCs can also be found in a number of states besides Florida, including Michigan, New Jersey, New York, Ohio, Pennsylvania, and Wisconsin.²⁴³ In Wisconsin, the county court supervises the process, and determines if a receiver will be appointed; issues injunctions against creditor actions; approves sales, distributions, and fees; hears preference and avoidance actions; and resolves controversies, including disputes over claims.²⁴⁴ Unlike in Florida, the assignment does not actually occur until it has been filed with the court and the case begins.²⁴⁵ In both Florida and Wisconsin, the court supervises the process; however, in Wisconsin, an ABC is considered to be a "special proceeding" rather than an action.²⁴⁶

236. *Id.*

237. *See id.* at 21.

238. *See id.* at 21 (citing FLA. STAT. § 727.108(4) (2007)). ("Previously, this section required court authorization for the assignee to conduct the business. This gave rise to a diverse practice in which some assignees moved ex parte and others moved upon notice and hearing. The confusion and delay in obtaining authorization, which was often detrimental to the estate, has been eliminated. Interested parties receive notice and may object to continued operation beyond fourteen days.").

239. FLA. STAT. § 727.108(4) (2007).

240. *Id.*

241. *See Davis, supra* note 38, at 21.

242. FLA. STAT. § 727.109(7) (2007).

243. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03; Richards & Ross, *supra* note 13, at 5.

244. WIS. STAT. ANN. § 128.01 (West 2009); JONATHAN FRIEDLAND, STRATEGIC ALTERNATIVES FOR AND AGAINST DISTRESSED BUSINESSES § 37.1 (2010).

245. FRIEDLAND, *supra* note 244, § 37.1.

246. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.3.

The Wisconsin ABC also creates an injunction against all other actions relating to the debtor's insolvency issues.²⁴⁷ Wisconsin requires the assignee to be a resident of Wisconsin, but does not define resident.²⁴⁸ The assignee must provide all creditors with prompt notice, publish the notice in the county where the proceeding is pending, and must provide notice of the injunction against all other actions and the time period for filing claims.²⁴⁹ Further, Wisconsin courts tend to enjoin single creditors from participation in ABCs. Hence, these ABCs are really only an option for small businesses.²⁵⁰

Advocates of the heavily regulated ABC form see it as giving the process a framework, enabling it to be more easily understood, more consistent with public policy, and better able to protect creditors.²⁵¹ Where heavily regulated ABCs go wrong, however, is by trying to work out the kinks of common law and minimally regulated ABCs to the detriment of the benefits that made ABCs as a process favorable in the first place. For example, heavily regulated ABCs require court filing and enable court involvement throughout the process.²⁵² While this may be viewed as presenting needed transparency for creditors because they are better able to challenge the assignee's actions, court filings can slow down the process by involving another actor and another hurdle to overcome.²⁵³ When the court is involved and filing is necessary throughout, ABCs can become a waiting game where assignees must wait for the court's response before they can act.²⁵⁴ This creates more lost opportunities, busier dockets, and more expenses on the already financially strained estate of the debtor.²⁵⁵

For example, Florida used to require court approval before the assignee could run the debtor's business.²⁵⁶ However, Florida recently revised this requirement after realizing it was hurting already financially-strapped companies because often by the time the court

247. FRIEDLAND, *supra* note 244, § 37.1; Eisenbach, *supra* note 9 (comparing this injunction to a stay under the Bankruptcy Code).

248. WIS. STAT. ANN. § 128.02 (West 2009).

249. FRIEDLAND, *supra* note 244, §§ 37.2, 37.4 (citing WIS. STAT. ANN. § 128.14 (West 2009)).

250. *Id.* § 37.4.

251. *See generally* Davis, *supra* note 38.

252. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03. On the other hand, court supervision can help reduce or eliminate factual disputes related to the assignment. *See* Verbrugge, *supra* note 30, at 10.

253. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

254. *See* Davis, *supra* note 38, at note 19.

255. *Id.* at 20.

256. *Id.* at 21.

had approved the assignee to run the business, much of the remaining value of the business had already decreased.²⁵⁷

In general, heavily regulated ABCs have comprehensive and detailed procedures for their administration.²⁵⁸ These procedures were created to solve prior problems that existed with less regulated forms. However, experience shows that what they really do is make the ABC process more cumbersome, more expensive, and more drawn-out, thus removing many of the benefits of using an ABC over bankruptcy.²⁵⁹

III. MAKING ABCs A VIABLE ALTERNATIVE TO BANKRUPTCY THROUGHOUT THE STATES

As addressed above, ABC reform is not a new idea.²⁶⁰ ABCs in all states started out as common law forms.²⁶¹ The almost complete freedom enjoyed by assignors and assignees at common law had a large potential for abuse, and led to many calls for reform.²⁶² Throughout the past century, many states enacted legislation and additional rules to address these issues.²⁶³ Over time, the ABC process became too widely varied by state and too cumbersome, and, as a result, ABCs were not widely used in many states.²⁶⁴

Despite their desuetude, ABCs can provide a more efficient way to address insolvency than bankruptcy in certain types of companies.²⁶⁵ As discussed in Part II, the success that an ABC sees depends on its maximizing its benefits over bankruptcy, and the frequency of its use depends on practitioner familiarity with its state's ABC process. To most legal practitioners, including even those specializing in bankruptcy, ABCs are an unfamiliar process.²⁶⁶ Accordingly, for ABCs to see more frequent use in all states, they need to be

257. *See id.*

258. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03 (“The majority [of heavily regulated ABC statutes] are fairly comprehensive, spelling out in detail who may make assignments, the requisites for a valid assignment, the role and duties of an assignee, what property may be included in an assigned estate, how an assigned estate is to be managed and administered, and the manner in which creditor’s claims are to be presented, proved and paid.”).

259. *See generally* Neiwirth & Bloom, *supra* note 227 (explaining how Florida’s ABC was revised and scaled back).

260. *See supra* Parts I.D, II.

261. *See* Choslovsky & Walker, *supra* note 11, at 93.

262. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

263. *Id.*

264. *See supra* Part I.D.

265. *See supra* Part I.C.

266. *See supra* Part I.D.

reformed, and that reform needs to be twofold.²⁶⁷ First, this Part argues that ABCs should be reformed across the states into an ABC that will maximize the benefits and minimize the disadvantages of ABCs. Second, it suggests that a minimally regulated ABC process would strike this balance because it is in the middle of the spectrum between common law and heavily regulated ABCs. This Part concludes by arguing that legal education about ABCs also needs to be reformed to include more instruction on ABCs.

A. States Need to Reform ABCs but Maintain Minimum Statutory Regulation

The lack of empirical data on ABCs makes it challenging to judge which ABC type is statistically the most successful or most popular. Further, since frequently used states' ABC processes do not all fall into the same category,²⁶⁸ it is difficult to conclude that one ABC form is a superior choice after which to model reform than another. However, comparing the advantages and disadvantages of each ABC group offers one way to find the best ABC form after which to model reform.

As previously mentioned, common law ABCs are not transparent enough.²⁶⁹ Because common law ABCs usually follow the form of the assignment, ABCs can vary extensively from one ABC to another even if taking place within the same state.²⁷⁰ Furthermore, practitioners must either be very familiar with their state's ABC process or must conduct extensive research before being able to conduct an ABC.²⁷¹ Research can be extremely time-consuming and expensive, undermining the efficiency associated with using an ABC.²⁷²

In addition, since debtors are the ones choosing to use ABCs over bankruptcy, the lack of transparency in common law ABCs may cause creditors to doubt the motives of debtors who are given a lot more freedom by ABCs.²⁷³ The fact that common law ABCs lack judicial

267. *See supra* Part I.D.

268. *See* Morrison, *supra* note 11, at 5.

269. *See supra* Part II.C.

270. *See* Davis, *supra* note 38, at 33.

271. *See* COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 16 (discussing the unfamiliarity of judges and clerks alike, and the necessary resulting research); *supra* Part II.C. *See generally* DEBTOR-CREDITOR LAW, *supra* note 29.

272. *Cf.* COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 16.

273. *See supra* Part II.A.

review prior to the completion of the ABC process only adds to creditors' concerns.²⁷⁴ Many creditors would prefer at least some oversight of the process, which minimally regulated ABCs can offer.²⁷⁵

Minimally regulated ABCs are by no means without problems.²⁷⁶ Given that minimally regulated ABCs differ greatly even from one another, however, it is very hard to summarize a shared list of disadvantages of minimally regulated ABCs.²⁷⁷ Rather, their advantages and disadvantages seem to result from where they fall on the spectrum of ABCs.²⁷⁸

Heavily regulated ABCs, on the other hand, often impose obligations on debtors that undercut the time- and cost- savings efficiencies of an ABC process, thus making their state's ABC have almost as many requirements and burdens as bankruptcy.²⁷⁹ For example, heavily regulated ABCs spell out in detail who may make assignments, the requisites for a valid assignment, the role and duties of an assignee, what property may be included, how the assigned estate is to be managed and administered, and much more.²⁸⁰ This reduces the amount of freedom and creativity an assignee may use in administering the estate and liquidating the assets.²⁸¹ Also, while heavy regulation may appear to give more security to creditors, it really makes the ABC process less efficient and resourceful with how it liquidates the assets, and thus a less attractive alternative to bankruptcy.²⁸²

In recent years, some states, including California and Florida, have revised their heavily regulated ABCs to remove unnecessary requirements, and as a result, have seen an uptick in reliance on their

274. See Scalabrino, *supra* note 71, at 264; cf. Choslovsky & Walker, *supra* note 11, at 93.

275. Depending on how you view the court's oversight abilities in ABCs, this can either be a major drawback or a major advantage. See Verbrugge, *supra* note 30, at 135 (noting that court supervision can help reduce or eliminate factual disputes related to the assignment).

276. See *supra* Part II.B.

277. See *supra* Part II.B.

278. See *supra* Part II.B. In other words, if a minimally regulated ABC falls close to the common law ABC line, it shares many of the same disadvantages as common law ABCs; on the other hand, if it falls closer to the heavily regulated ABC line, it no longer has the disadvantages of a common law ABC but rather has the disadvantages of a heavily regulated ABC.

279. See *supra* Part II.C.

280. See *supra* Part II.C.

281. See *supra* Part II.C.

282. See *supra* Part II.C.

state's ABCs.²⁸³ Additionally, California has been called by multiple sources "the capital of ABCs," and many recent articles on the subject matter center their discussions on California ABCs.²⁸⁴ California has experienced all three categories of ABCs.²⁸⁵ The state replaced its common law ABC with a heavily regulated ABC only to realize that a heavily regulated form detracted from many of the attractive qualities of ABCs.²⁸⁶ In response, the California legislature repealed the heavily regulated ABC and returned to a hybrid form of ABC that was mainly based in common law.²⁸⁷ However, they enacted "supplementary statutes" to address specific aspects of ABCs that had been seen to cause confusion without regulations, such as notice requirements.²⁸⁸

While Florida was categorized into the heavily regulated ABC, the reasons behind Florida's ABC reform resonate with why reform in all states is a beneficial idea.²⁸⁹ The reforms were meant to make the process run smoothly and more efficiently by removing needless burdens.²⁹⁰ Florida believed that having a uniform ABC procedure, rather than a common law ABC, would enable more practitioners to understand and use ABCs in the future.²⁹¹ Therefore, while it did not completely abolish its court-filing and authorization requirements, it decreased the amount of court involvement.²⁹² Although these reforms did not necessarily categorize Florida's ABC as minimally regulated, Florida's reforms reveal that heavily regulated ABCs can go too far. To avoid the dangers of becoming too regulated while avoiding the problems of common law ABCs, states should rely on an ABC standard similar to the one that this Note refers to as "minimally regulated."²⁹³

283. *See supra* Part II.

284. *See, e.g.,* David Kupetz, *For Bankruptcy Alternative, Know Your 'ABCs'*, TURNAROUND MGMT. ASS'N (July 1, 2003), <https://www.turnaround.org/Publications/Articles.aspx?objectID=2190>.

285. *See supra* Part II.B.

286. *See supra* Part II.B.

287. *See supra* Part II.B.

288. *See supra* Part II.B.

289. *See supra* Part II.C.

290. *See generally* Verbrugge, *supra* note 30; *supra* Part II.C.

291. *See* Davis, *supra* note 38, at 18–19.

292. *See supra* Part II.C.

293. *See supra* Part II.B.

**B. While Minimally Regulated ABCs Are Not Perfect, they
Provide the Best Opportunity for ABCs to See More Frequent
Use**

Minimally regulated ABCs exist on a wide spectrum. Some minimally regulated ABCs appear to be almost completely common law based, while others appear to be very similar to heavily regulated ABCs.²⁹⁴ However, minimally regulated ABCs represent the best of both categories. They can avoid the lack of transparency in common law ABCs, while also avoiding the over-cumbersomeness of heavily regulated ABCs.²⁹⁵ Minimally regulated ABCs generally follow a common law format to some extent but have statutes that help structure the process.²⁹⁶ This helps make the process more transparent, and should put creditors more at ease with a debtor's choice of using an ABC over a bankruptcy. Furthermore, regulation of an ABC might be minimal while still providing the best protections afforded by heavily regulated ABCs. For example, filing requirements enable data collection, which at very least permits policymakers to keep track of ABCs.²⁹⁷ Data collection improves the court's ability to review an ABC, and it will assist scholars in better forming opinions about ABCs and legislatures in adjusting their ABC laws.²⁹⁸ Furthermore, collecting more data using better methods has little downside because it adds little expense to the process itself and does not restrain the assignee's practices.²⁹⁹

Furthermore, advocating for reforming to a minimally regulated ABC process gives states options when reforming their ABC processes.³⁰⁰ While minimally regulated ABCs avoid many of the problems of common law ABCs and heavily regulated ABCs, minimally regulated ABCs are not perfect. Some forms of minimally regulated ABCs may be better than others.³⁰¹

Since California's ABC is arguably the most successful in the nation, states looking to reform their ABC should look to California's

294. *See supra* Part II.B

295. *See supra* Part II.B

296. *See* DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03; Chatz & Levy, *supra* note 118, at 4; Choslovsky & Walker, *supra* note 11, at 91.

297. *See* Mann, *supra* note 22, at 1396.

298. *Id.*

299. *Id.*

300. Since minimally regulated ABCs fall across a wide spectrum, there is a lot of variety in how minimally regulated ABCs are found and can be structured. *See supra* Part II.B.

301. *See supra* Part II.B.

ABC for guidance.³⁰² As mentioned previously, the success of California's ABC is not limited to the dot-com industry.³⁰³ It is not the type of company that makes ABCs a viable solution; it is the form of the solution itself that makes California's ABC work.³⁰⁴ California's ABC is extremely assessable, and it is not overly burdensome in requirements.³⁰⁵

States reforming to minimally regulated ABCs should also enact supplementary statutes, like California, in order to address common problems that occur within their state.³⁰⁶ Through supplementary statutes, states can give courts some form of oversight, up to that state's discretion.³⁰⁷ However, states ought to structure the amount of court involvement by attempting to avoid pushing their ABC into heavily regulated ABC territory.³⁰⁸

In sum, minimally regulated ABCs provide the best solution to making ABCs see more frequent use. They require low court involvement and have minimal requirements and hindrances to the process.³⁰⁹ Minimally regulated ABCs give debtors and assignees enough flexibility in forming an assignment to maximize the time- and cost-efficient benefits of ABCs, while minimizing the fears of creditors that debtors and assignees have too much freedom. Finally, they enhance the benefits of ABCs over bankruptcy while minimizing the drawbacks. Therefore, when reforming its ABC process, a state should strive to achieve a minimally regulated ABC form.

C. Legal Education, Including Law School Classes and CLE Programs, Ought to Adjust Their Curriculum to Include Instruction on ABCs in Order to Make Reforms as Successful as Possible and Make ABCs an Alternative to Be Considered

Before the benefits of minimally regulated ABCs as a format can be realized, ABCs, their processes, and the need for reform first need to come to the attention of the legal community at large. ABCs currently lack "the institutional formality and widespread familiarity

302. *See supra* Part II.B. Further, since California's ABC has itself undergone reform in order to maximize its usage and benefits, it provides an excellent model for reform. *See* Luo, *supra* note 15, at 524.

303. *See* Mann, *supra* note 22, at 1390.

304. *See supra* Parts I, II.

305. *See supra* Part II.B.

306. *See supra* Part II.B.

307. *See supra* Part II.B.

308. For guidance on what constitutes "heavily regulated," *see supra* Part II.C.

309. *See supra* Part II.B.

of a formal bankruptcy proceeding” because they are infrequently used.³¹⁰ Once reform occurs, ABC will have institutional formality.³¹¹ Reforming the process, however, cannot in itself create widespread familiarity, which is necessary for ABCs to be truly successful on a more widespread scale.³¹² The frequency with which ABCs are used depends as much upon the choice of practitioners as it does on the form of ABC.

Therefore, to create widespread familiarity, ABCs should be incorporated into legal education. Whether ABCs are just taught in a day of a bankruptcy course or make up their own course, law schools need to incorporate ABCs into their curriculum. In addition, if states add ABCs to their bar exams, ABCs would undoubtedly become more well-known. Furthermore, Continuing Legal Education (CLE) courses ought to incorporate ABCs into their discussions to inform current practitioners on the possibility of using ABCs as an alternative to bankruptcy. Legal practitioners will be the ones who ultimately choose the fate of any reformed ABC and how frequently it is used, so their knowledge of the process is crucial. Hence, before any reform will be successful, practitioners need to become aware that ABCs are another way to deal with an insolvent company, and ABCs may be preferable to bankruptcy and other alternatives to it, in some cases.

CONCLUSION

For some insolvent companies ABCs are a great alternative to bankruptcy because they can be more time efficient, less costly, and less public than bankruptcy.³¹³ Although ABCs have these benefits in certain situations, ABCs are found in many different forms; thus these advantages over bankruptcy are not found in every state’s ABC process.³¹⁴ Further, some states’ ABCs see more frequent use than other states where ABCs are rarely, if ever, used.³¹⁵ ABC reform across all states would benefit insolvent companies by providing an accessible alternative to bankruptcy.

310. See COMM. ON BANKRUPTCY & CORPORATE REORGANIZATION, *supra* note 15, at 16. See generally, DEBTOR-CREDITOR LAW, *supra* note 29, § 35.03.

311. See Berman & Vance, *supra* note 27, at 33–34 (proposing a model statute that would lessen the state by state diversity of ABCs and make the process more uniform).

312. See generally *id.* (discussing how a proposed model statute aimed to make the ABC process more uniform and, in turn, more utilized on a nationwide basis.).

313. See *supra* Part I.

314. See *supra* Part I.

315. See *supra* Parts I, II.

Although it may be expected that one type of ABC might be used more frequently than another, no one ABC category encompasses all the frequently used ABC processes.³¹⁶ In other words, while one ABC form may maximize the advantages of ABCs better than another, the type of the ABC is currently not enough to determine whether that state's ABC sees frequent use or not.³¹⁷ For example, while California's minimally regulated ABC saw frequent use, many other states with minimally regulated ABCs saw little to no use.³¹⁸ Despite this incongruity, this Note still concludes that minimally regulated ABCs offer the best model for reform because they best maximize the benefits of ABCs while avoiding many of the disadvantages found in common law and heavily regulated ABCs.

However, before ABCs can be more frequently used nationwide, reform efforts cannot stop at reforming the ABC process itself. Reform also needs to reach into law schools and CLE programs to inform lawyers about ABCs. If ABCs were better incorporated into legal instruction, practitioners would be more familiar with the process, and would be more likely to consider using ABCs as an alternative to bankruptcy. Once these reforms take place and knowledge about ABCs is more widespread, ABCs will be able to truly reach their potential as a beneficial alternative to bankruptcy.

316. *See supra* Part II.

317. *See supra* Part II.

318. *See supra* Part II.